

DEPARTMENT OF DEFENSE**GENERAL SERVICES
ADMINISTRATION****NATIONAL AERONAUTICS AND
SPACE ADMINISTRATION****48 CFR Parts 15, 42, 46, 47 and 52**

[FAR Case 95-022]

RIN 9000-AH27

**Federal Acquisition Regulation;
Changes in Contract Administration
and Audit Cognizance**

AGENCIES: Department of Defense (DOD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Proposed rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council are proposing to amend the Federal Acquisition Regulation (FAR) to add policies and procedures for assigning and performing contract audit services and to clarify the policy for assigning or delegating responsibility for establishing forward pricing and billing rates, and final indirect cost rates. This regulatory action was not subject to Office of Management and Budget review under Executive Order 12866, dated September 30, 1993. This is not a major rule under 5 U.S.C. 804.

DATES: Comments should be submitted on or before February 10, 1997 to be considered in the formulation of a final rule.

ADDRESSES: Interested parties should submit written comments to: General Services Administration, FAR Secretariat (MVRs), 18th & F Streets, NW, Room 4037, Washington, DC 20405.

E-mail comments submitted over Internet should be addressed to: 95-022@www.arnet.gov.

Please cite FAR case 95-022 in all correspondence related to this case.

FOR FURTHER INFORMATION CONTACT: Ms. Linda Klein at (202) 501-3775 in reference to this FAR case. For general information, contact the FAR Secretariat, Room 4037, GS Building, Washington, DC 20405 (202) 501-4755. Please cite FAR case 95-022.

SUPPLEMENTARY INFORMATION:**A. Background**

In February 1994, the Office of Federal Procurement Policy formed a Contract Audit Committee. The committee was divided into

subcommittees. This case implements recommendations of Subcommittee One to address civilian agencies' contract administration and audit practices. The rule amends FAR Parts 15, 42, 46, 47 and 52 to add policies and procedures for assigning and performing contract audit services and to clarify the policy for assigning or delegating responsibility for establishing forward pricing and billing rates, and final indirect cost rates.

B. Regulatory Flexibility Act

This proposed rule is not expected to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because the proposed rule affects primarily internal Government operating procedures. An Initial Regulatory Flexibility Analysis has, therefore, not been performed. Comments from small entities concerning the affected FAR parts will be considered in accordance with 5 U.S.C. 610 of the Act. Such comments must be submitted separately and should cite 5 U.S.C. 601, *et seq.* (FAR case 95-022), in correspondence.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the proposed changes to the FAR do not impose recordkeeping or information collection requirements, or collections of information from offerors, contractors, or members of the public which require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 15, 42, 46, 47 and 52

Government procurement.

Dated: December 4, 1996.

Edward C. Loeb,

Director, Federal Acquisition Policy Division.

Therefore, it is proposed that 48 CFR Parts 15, 42, 46, 47 and 52 be amended as set forth below:

1. The authority citation for 48 CFR Parts 15, 42, 46, 47 and 52 continues to read as follows:

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

**PART 15—CONTRACTING BY
NEGOTIATION**

2. Section 15.809 is amended by revising the section heading and the last sentence in paragraph (a) to read as follows:

15.809 Forward pricing rate agreements.

(a) * * * The cognizant Federal agency (see 42.003) shall determine whether an FPRA will be established.

* * * * *

**PART 42—CONTRACT
ADMINISTRATION AND AUDIT
SERVICES**

3. Part 42 heading is revised to read as shown above.

4. Section 42.000 is revised and placed in a new subpart 42.0, which is added to read as set forth below, and subparts 42.1 and 42.2 are revised to read as follows:

Sec.

Subpart 42.0—General

42.000 Scope of part.
42.001 Definitions.
42.002 Interagency agreements.
42.003 Cognizant Federal agency.

Subpart 42.1—Contract Audit Services

42.101 Contract audit responsibilities.
42.102 Assignment of audit services.
42.103 Audit services directory.

**Subpart 42.2—Contract Administration
Services**

42.201 Contract administration responsibilities.
42.202 Assignment of contract administration.
42.203 Contract administration services directory.

Subpart 42.0—General**42.000 Scope of part.**

This part prescribes policy and procedures for assigning and performing contract administration and contract audit services.

42.001 Definitions.

As used in this part—

Cognizant audit agency means the agency responsible for performing all required contract audit services at a business unit (as defined in 31.001).

Cognizant Federal agency means the Federal agency that on behalf of all Federal agencies is responsible for establishing final indirect cost rates and forward pricing rates, if applicable, and administering cost accounting standards for all contracts in a business unit.

42.002 Interagency agreements.

(a) Agencies shall avoid duplicate audits, reviews, inspections, and examinations of contractors or subcontractors, by more than one agency, through the use of interagency agreements (see OFPP Policy Letter 78-4, Field Contract Support Cross-Servicing Program).

(b) Subject to the fiscal regulations of the agencies, the requesting agency may reimburse the servicing agency for rendered services in accordance with the Economy Act of 1932 (31 U.S.C. 1535). The hourly rate established under the interagency agreement between the Department of Defense and the National Aeronautics and Space Administration may be used by other agencies to reimburse the Defense Contract Audit Agency for audit services.

(c) When an interagency agreement is established, the agencies are encouraged to consider establishing procedures for the resolution of issues that may arise under the agreement.

42.003 Cognizant Federal agency.

(a) Normally, when a contractor has contracts with more than one agency, the agency with the largest dollar amount of negotiated contracts should be the cognizant Federal agency.

(b) Once a Federal agency assumes cognizance for a contractor, it shall remain cognizant for at least three years to ensure continuity and ease of administration. If, at the end of the three years, another agency has the largest dollar amount of negotiated contracts, the two agencies shall coordinate and determine which will assume cognizance.

Subpart 42.1—Contract Audit Services

42.101 Contract audit responsibilities.

(a) The auditor is responsible for submitting information and advice to the requesting activity based on the auditor's analysis of the contractor's financial and accounting records or other related data as to the acceptability of the contractor's incurred and estimated costs, as well as for reviewing the financial and accounting aspects of the contractor's cost control systems. The auditor is also responsible for performing analyses and reviews which require access to the contractor's financial and accounting records supporting proposed and incurred costs.

(b) The Defense Contract Audit Agency (DCAA) is designated as the Government cognizant audit agency for "for-profit" organizations and those "not-for-profit" organizations identified in Attachment C to OMB Circular A-122, Cost Principles for Nonprofit Organizations.

42.102 Assignment of audit services.

(a) As provided in agency procedures or interagency agreement, contracting officers may request audit services directly from the cognizant audit agency cited in the Directory of Federal Contract Audit Offices. The audit

request should include a suspense date and identify any information needed by the contracting officer.

(b) The cognizant audit agency may decline requests for services in accordance with interagency agreements on a case-by-case basis if resources of the audit agency are inadequate to accomplish the tasks.

42.103 Audit services directory.

(a) DCAA maintains and distributes the Directory of Federal Contract Audit Offices. The directory identifies cognizant audit offices and the contractors over which they have cognizance. Changes to audit cognizance are to be provided to DCAA for updating the directory.

(b) Agencies may obtain a copy of the directory or obtain information concerning cognizant audit offices by contacting the Defense Contract Audit Agency, ATTN: CMO, Publications Officer, 8725 John J. Kingman Road, Suite 2135, Fort Belvoir, Virginia 22060-6219.

Subpart 42.2—Contract Administration Services

42.201 Contract administration responsibilities.

(a) For each contract assigned for administration, the contract administration office (CAO) (see definition at 2.101) shall—

(1) Perform the functions listed in 42.302(a) to the extent that they apply to the contract, except for the functions specifically withheld;

(2) Perform the functions listed in 42.302(b) only when and to the extent specifically authorized by the contracting officer; and

(3) Request supporting contract administration under 42.202(e), and (f) when it is required.

(b) The Defense Logistics Agency, Defense Contract Management Command (DCMC), Fort Belvoir, Virginia, and certain civilian agencies offer a wide variety of contract administration and support services to other agencies.

42.202 Assignment of contract administration.

(a) *Delegating functions.* As provided in agency procedures, contracting officers may delegate contract administration or specialized support services either through interagency agreements, or by direct request to the cognizant CAO listed in the Federal Directory of Contract Administration Services Components. The delegation should include—

(1) The name and address of the CAO designated to perform the

administration (this information is also to be entered in the contract);

(2) Any special instructions, including any specific authorization to perform functions listed in 42.302(b);

(3) A copy of the contract to be administered; copies of all contracting agency regulations or directives that are—

(i) Incorporated into the contract by reference, or

(ii) Otherwise necessary to administer the contract, unless copies have been provided previously.

(b) *Special instructions.* The contracting officer shall also advise the CAO and the contractor (and other activities as appropriate) of any functions withheld or additional functions delegated in the special instructions under paragraph (a)(2) of this section.

(c) *Delegating additional functions.* For individual contracts or groups of contracts, the contracting office may delegate to the CAO functions not listed in 42.302; provided that—

(1) Prior coordination with the CAO ensures the availability of required resources;

(2) In the case of authority to issue orders under provisioning procedures in existing contracts and under basic ordering agreements for items and services identified in the schedule, the head of the contracting activity or designee approves the delegation; and

(3) The delegation does not require the CAO to undertake new or follow-on acquisitions.

(d) *Rescinding functions.* The contracting officer of the requesting agency may rescind or recall a contract or contract administration function delegated to another agency for administration, except for cost accounting standards, and negotiation of forward pricing rates and indirect cost rates (see 42.003).

(e) *Secondary delegations of contract administration.* (1) A CAO delegated administration of a contract under 42.202(a) or (c), or a contracting office retaining administration, may request supporting contract administration from the CAO cognizant of the contractor location where performance of specific contract administration functions is required. The request shall—

(i) Be in writing;

(ii) Clearly state the specific functions to be performed; and

(iii) Be accompanied by a copy of pertinent contractual and other necessary documents.

(2) The prime contractor is responsible for managing its subcontracts. The CAO's review of subcontracts is normally limited to

evaluating the prime contractor's management of them (see part 44). Therefore, supporting contract administration shall not be used for subcontracts unless—

(i) The Government would otherwise incur undue cost;

(ii) Successful completion of the prime contract is threatened; or

(iii) It is authorized under paragraph (f) of this section or elsewhere in this part.

(f) *Special surveillance.* For major system acquisitions (see part 34), the contracting officer may designate certain high risk or critical subsystems or components for special surveillance in addition to requesting supporting contract administration. This surveillance shall be conducted in a manner consistent with the policy of calling upon the cognizant CAO to perform contract administration functions at a contractor's facility (see 42.002).

(g) *Refusing delegation of contract administration.* An agency may decline a request for contract administration services on a case-by-case basis if resources of the agency are inadequate to accomplish the tasks.

42.203 Contract administration services directory.

The Defense Contract Management Command (DCMC) maintains and distributes the Federal Directory of Contract Administration Services Components. The Directory lists the name and telephone number of those DCMC and civilian agency offices which offer contract administration services within designated geographic areas and at specified contractor plants. Federal agencies may obtain a free copy of the Directory on CD-ROM by writing to HQ Defense Logistics Agency, Attn: DLA-DASC-WP, 8725 John J. Kingman Road, Fort Belvoir, Virginia 22060.

5.–7. Section 42.301 is revised to read as follows:

42.301 General.

When a contract is assigned for administration under Subpart 42.2, the contract administration office (CAO) shall perform contract administration functions in accordance with this part, the contract terms and, unless otherwise agreed to in an interagency agreement (see 42.002), the applicable regulations of the servicing agency.

8. Section 42.302 is amended by revising paragraphs (a) introductory text, (a)(9), (a)(11) introductory text, (a)(11)(iv), (a)(13), (a)(20), (a)(29), (a)(61) (a)(63) and (b) introductory text to read as follows:

42.302 Contract administration functions.

(a) The following contract administration functions are normally delegated to a CAO. The contracting officer may retain any of these functions, except those in paragraphs (a) (5), (9), and (11) that cannot be retained by the awarding agency unless it is the cognizant Federal agency (see 42.001).

(9) Establish final indirect cost rates and billing rates for those contractors meeting the criteria for contracting officer determination in subpart 42.7 (see 42.001).

(11) In connection with Cost Accounting Standards (see 30.601, 42.001, and 48 CFR chapter 99 (FAR Appendix B))—

(iv) Negotiate price adjustments and execute supplemental agreements under the Cost Accounting Standards clauses at 52.230–2, 52.230–3, 52.230–4, 52.230–5, and 52.230–6.

(13) Make payments on assigned contracts when prescribed in agency acquisition regulations.

(20) For classified contracts, administer those portions of the applicable industrial security program delegated to the CAO (see subpart 4.4).

(29) Issue contract modifications requiring the contractor to provide packing, crating, and handling services on excess Government property. When the CAO determines it to be in the Government's interests, the services may be secured from a contractor other than the contractor in possession of the property.

(61) Obtain contractor proposals for any contract price adjustments resulting from amended shipping instructions. CAOs shall review all amended shipping instructions on a periodic, consolidated basis to assure that adjustments are timely made. Except when the CAO has settlement authority, the CAO shall forward the proposal to the contracting officer for contract modification. The CAO shall not delay shipments pending completion and formalization of negotiations of revised shipping instructions.

(63) Cancel unilateral purchase orders when notified of nonacceptance by the contractor. The CAO shall notify the contracting officer when the purchase order is canceled.

(b) The CAO shall perform the following functions only when and to the extent specifically authorized by the contracting office:

* * * * *

9. Section 42.602 is amended by revising paragraphs (c)(2) and (d) to read as follows:

42.602 Assignment and location.

* * * * *

(c) * * *

(2) When the locations are under the contract administration cognizance of more than one agency, the agencies concerned shall agree on the responsible agency (normally on the basis of the agency with the largest dollar balance of affected contracts). In such cases, agencies may sometimes also consider geographic location.

(d) The directory of contract administration components referenced in 42.203 includes a listing of CACO's and the contractors for which they are assigned responsibility.

10. Section 42.603(a) is revised to read as follows:

42.603 Responsibilities.

(a) The CACO shall perform, on a corporate-wide basis, the contract administration functions as designated by the responsible agency. Typical CACO functions include—

(1) The determination of final indirect cost rates for cost-reimbursement contracts,

(2) Establishment of advance agreements or recommendations on corporate/home office expense allocations, and

(3) Administration of Cost Accounting Standards (CAS) applicable to corporate-level and corporate-directed accounting practices.

* * * * *

11. Section 42.701 is amended by revising definitions for "Business unit" and "Indirect cost" and by adding in alphabetical order a definition for "Forward pricing rate agreement". The revised and added text reads as follows:

42.701 Definitions.

* * * * *

Business unit has the same meaning as defined in 31.001.

* * * * *

Forward pricing rate agreement has the same meaning as defined in 15.801.

Indirect cost has the same meaning as defined in 31.203.

* * * * *

12. Section 42.703–1 is amended by revising paragraph (a), and by removing paragraph (c) introductory text, and revising (c)(1) to read as follows:

42.703-1 Policy.

(a) A single agency (see 42.705-1) shall be responsible for establishing final indirect cost rates for each business unit. These rates shall be binding on all agencies and their contracting offices, unless otherwise specifically prohibited by statute.

* * * * *

(c)(1) Final indirect cost rates shall be used for contract closeout for a business unit unless the quick-closeout procedure in 42.708 is used. These final rates shall be binding for all cost-reimbursement contracts at the business unit, subject to any specific limitation in a contract or advance agreement; and

* * * * *

13. Section 42.704 is amended by revising paragraphs (a), (b), and (c) to read as follows:

42.704 Billing rates.

(a) The contracting officer (or cognizant Federal agency official) or auditor responsible under 42.705 for establishing the final indirect cost rates ordinarily shall also be responsible for determining the billing rates.

(b) The contracting officer (or cognizant Federal agency official) or auditor shall establish billing rates on the basis of information resulting from recent review, previous rate audits or experience, or similar reliable data or experience of other contracting activities. In establishing billing rates, the contracting officer (or cognizant Federal agency official) or auditor should ensure that they are as close as possible to the final indirect cost rates anticipated for the contractor's fiscal period, as adjusted for any unallowable costs. When the contracting officer (or cognizant Federal agency official) or auditor determines that the dollar value of contracts requiring use of billing rates does not warrant submission of a detailed billing rate proposal, the billing rates may be established by making appropriate adjustments from the prior year's indirect cost experience to eliminate unallowable and nonrecurring costs and to reflect new or changed conditions.

(c) Once established, billing rates may be prospectively or retroactively revised by mutual agreement of the contracting officer (or cognizant Federal agency official) or auditor and the contractor at either party's request, to prevent substantial overpayment or underpayment. When agreement cannot be reached, the billing rates may be unilaterally determined by the contracting officer (or cognizant Federal agency official).

* * * * *

14. Section 42.705-1 is amended by revising paragraphs (a) introductory text, (a) (1), (3) and (4) and (b) (1) and (2) to read as follows:

42.705-1 Contracting officer determination procedure.

(a) *Applicability and responsibility.* Contracting officer determination shall be used for the following, with the indicated cognizant contracting officer (or cognizant Federal agency official) responsible for establishing the final indirect cost rates:

(1) Business units of a multi-divisional corporation under the cognizance of a corporate administrative contracting officer (CACO) (see subpart 42.6), with that officer responsible for the determination, assisted, as required, by the administrative contracting officers, assigned to the individual business units. Negotiations may be conducted on a coordinated or centralized basis, depending upon the degree of centralization within the contractor's organization.

* * * * *

(3) For business units not included in paragraph (a)(1) or (a)(2) of this subsection, the contracting officer (or cognizant Federal agency official) will determine whether the rates will be contracting officer or auditor determined.

(4) Educational institutions (see 42.705-3.).

* * * * *

(b) *Procedures.* (1) In accordance with the Allowable Cost and Payment clause at 52.216-7 or 52.216-13, the contractor shall submit to the contracting officer (or cognizant Federal agency official) and, if required by agency procedures, to the cognizant auditor a final indirect cost rate proposal reflecting actual cost experience during the covered period, together with supporting cost or pricing data.

(2) The auditor shall submit to the contracting officer an advisory audit report—

(i) Identifying any relevant advance agreement or restrictive terms of specific contracts, and

(ii) Including the information required by 15.805-5(e) (1) and (2).

* * * * *

15. Section 42.705-2 is amended by revising paragraphs (a)(2) introductory text, (a)(2)(iv), (b)(2) introductory text, and (b)(2) (i), (ii), and (iv) to read as follows:

42.705-2 Auditor determination procedure.

(a) * * *

(2) In addition, auditor determination may be used for business units that are

covered in 42.705-1(a) when the contracting officer (or cognizant Federal agency official) and auditor agree that the indirect costs can be settled with little difficulty and any of the following circumstances apply:

* * * * *

(iv) The contracting officer (or cognizant Federal agency official) and auditor agree that special circumstances require auditor determination.

(b) *Procedures.* (1) * * *

(2) Upon receipt of proposal the auditor shall—

(i) Audit the proposal and seek agreement on indirect costs with the contractor;

(ii) Prepare an indirect cost rate agreement conforming to the requirements of the contracts. The agreement shall be signed by the contractor and the auditor;

* * * * *

(iv) If agreement with the contractor is not reached, forward the audit report to the contracting officer (or cognizant Federal agency official) identified in the Directory of Contract Administration Services Components (see 42.203), who will then resolve the disagreement; and

* * * * *

PART 46—QUALITY ASSURANCE

16. Section 46.103 is amended by revising paragraph (d) to read as follows:

46.103 Contracting office responsibilities.

* * * * *

(d) When contract administration is retained (see 42.201), verifying that the contractor fulfills the contract quality requirements; and

* * * * *

17. Section 46.104 is amended by revising paragraph (f) to read as follows:

46.104 Contract administration office responsibilities.

* * * * *

(f) Recommend any changes necessary to the contract, specifications, instructions, or other requirements that will provide more effective operations or eliminate unnecessary costs (see 46.103(c)).

18. Section 46.502 is amended by revising the second sentence to read as follows:

46.502 Responsibility for acceptance.

* * * When this responsibility is assigned to a cognizant contract administration office or to another agency (see 42.202(g)), acceptance by that office or agency is binding on the Government.

47.301-3 Using the Defense
Transportation System (DTS)

19. Section 47.301-3 is amended in paragraph (c) by removing “42.202(d)” and inserting “42.202(a)”.

PART 52—SOLICITATION PROVISIONS
AND CONTRACT CLAUSES

20. Section 52.216-7 is amended by revising the clause date and the first sentence of paragraph (d)(2) to read as follows:

52.216-7 Allowable Cost and Payment.

* * * * *

Allowable Cost and Payment (Date)

* * * * *

(d) Final indirect cost rates. (1) * * *

(2) The Contractor shall, within 90 days after the expiration of each of its fiscal years, or by a later date approved by the Contracting

Officer, submit to the cognizant Contracting Officer (or cognizant Federal agency official) responsible for negotiating its final indirect cost rates and, if required by agency procedures, to the cognizant audit activity proposed final indirect cost rates for that period and supporting cost data specifying the contract and/or subcontract to which the rates apply. * * *

* * * * *

(End of clause)

21. Section 52.216-13 is amended by revising the clause date and paragraph (c)(2) to read as follows:

52.216-13 Allowable Cost and Payment—
Facilities.

* * * * *

Allowable Cost and Payment—Facilities
(Date)

* * * * *

(c) Negotiated indirect costs. (1) * * *

(2) The Contractor shall, within 90 days after the expiration of each of its fiscal years, or by a later date approved by the Contracting Officer, submit to the Contracting Officer (or cognizant Federal agency official) and to the cognizant audit activity proposed final indirect cost rates for that period and supporting cost and data specifying the contract and/or subcontract to which the rates apply. The proposed rates shall be based on the Contractor’s actual cost experience for the period. The appropriate Government representative and the Contractor shall establish the final indirect cost rates as promptly as practical after receipt of the Contractor’s proposal.

* * * * *

(End of clause)

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